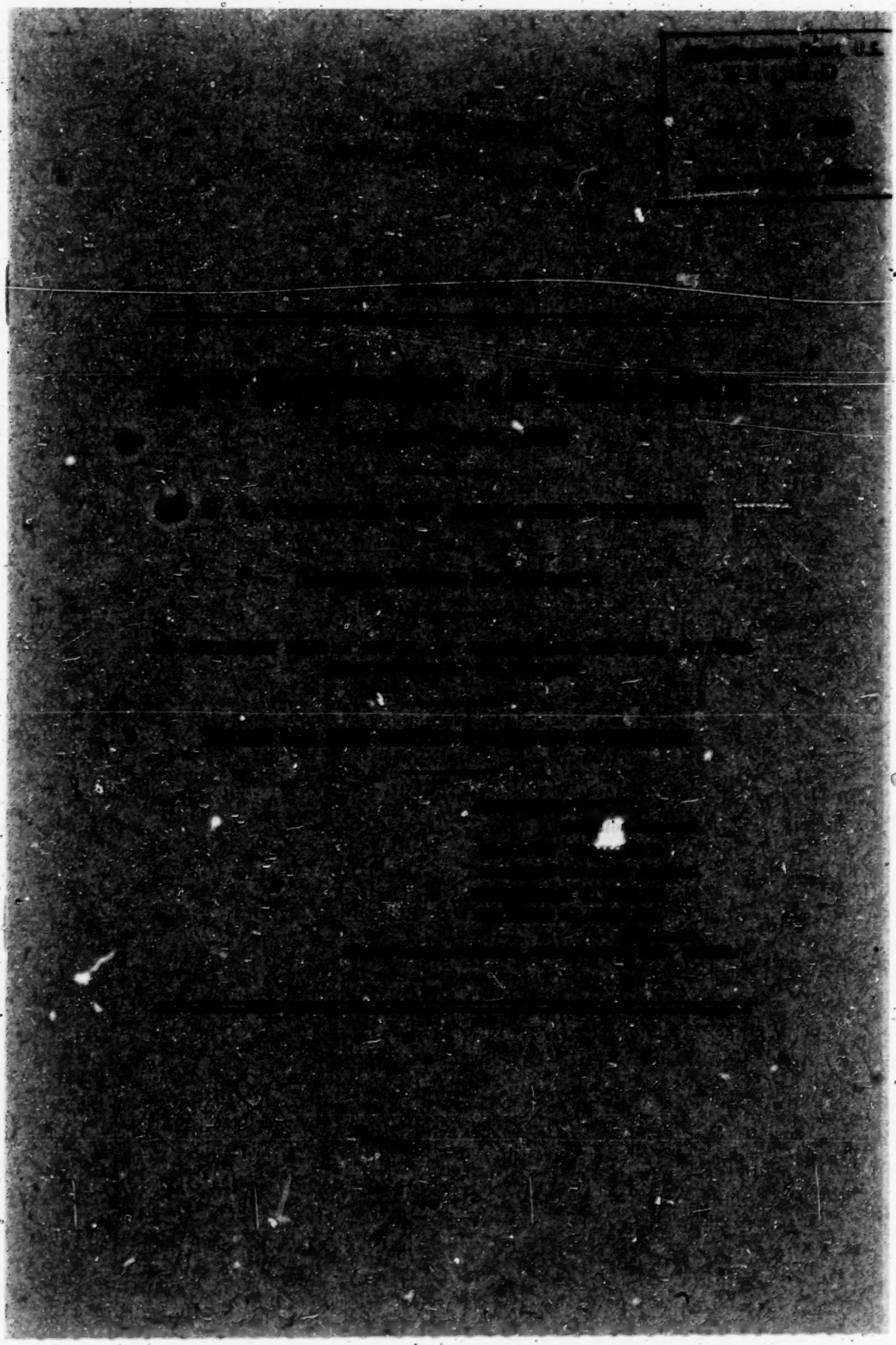

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In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 538

G. L. CHRISTIAN AND ASSOCIATES, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The original opinion of the Court of Claims, which was entered on January 11, 1963 (Pet. App. 2a–20a), is reported at 312 F. 2d 418. The opinion of the Court of Claims on a timely motion for rehearing, entered on July 12, 1963 (Pet. App. 69a–87a), is reported at 320 F. 2d 345.

JURISDICTION

The judgment of the Court of Claims denying petitioner's motion for rehearing and reargument was entered July 12, 1963. The petition for a writ of certiorari was filed on October 10, 1963. The jurisdiction of this Court is invoked under 28 U.S.C. 1255.

QUESTIONS PRESENTED

1. Whether § 8.703 of the Armed Services Procurement Regulations, which directs that a standard clause permitting termination for the convenience of the government "shall be inserted" in certain fixed-price government construction contracts, incorporates the termination clause into each of the specified contracts by operation of law, whether or not it is included by the parties.

2. Whether § 8.703, if self-operative, is authorized by statute.

3. Whether § 8.703 extends to construction contracts under the Capehart Act, 69 Stat. 646.

REGULATIONS AND CONTRACTUAL PROVISIONS INVOLVED

The pertinent portions of the Armed Services Procurement Regulations (ASPR) are set forth in Appendix B to the petition (Pet. App. 97a–98a). Pertinent excerpts from the construction contract are set forth in the Appendix hereto (p. 13, *infra*).

STATEMENT

This case arises out of the decision made by the Department of the Army in 1958 to deactivate Fort Polk, Louisiana. At the time of this decision, construction had commenced on 2,000 housing units to be used by military personnel at Fort Polk (Pet. App. 21a, 28a–29a, 37a). On February 5, 1958, when work on the project was 2.036 per cent complete, the con-

tractor[1] was notified that the contract, which called for a total price of over $32 million, was terminated for the convenience of the government (Pet. 37a, 42a, 44a). Claims for moneys already expended on the project by the contractor and the sub-contractors, plus the the profit earned thereon, have been either settled administratively (Pet. App. 56a–62a) or adjudicated by the Court of Claims (Pet. App. 63a–68a). At issue here is the Court of Claims' denial of anticipated profits which the contractor and the sub-contractors would have earned on the uncompleted portion of the project had the government not terminated the contract.

The project was being constructed under the Capehart Act (Title VIII of the National Housing Act), 63 Stat. 570, 69 Stat. 651, as amended, 12 U.S.C. 1748–1748g, 1720(f), 42 U.S.C. 1594–1594f, which expired on October 1, 1962, and has not been renewed, 76 Stat. 418, amending 12 U.S.C. 1748b(a). The Capehart Act procedure, more fully described in the Court of Claims' opinion (Pet. App. 13a, n.9), involved construction of the project by a private contractor, who would borrow funds from a

[1] G. L. Christian and Associates, although nominally the contractor and the petitioner here, in fact has no financial interest in the outcome, having in effect assigned its interest in the contract to a joint venture consisting of H. B. Zachry Company and Centex Construction Company, Inc. This joint venture is the real party in interest in this litigation, and all references herein to "petitioner" and "contractor" refer to it. The situation is explained more fully in Part I of the Court of Claims' opinion (Pet. App. 3a–10a).

private financial institution to cover both expenses of construction and his own profit. Until completion of construction, the mortgage taken by the private financial institution would be guaranteed by the Federal Housing Commissioner. Upon completion of the project, the government would assume the mortgage and would service it out of funds appropriated to pay the housing allowances of personnel assigned quarters in the project buildings.

The Housing Contract (Pltf. Ex. No. 8[2]), to which petitioner was a party, did not contain any provision expressly authorizing either party to terminate the contract (Pet. App. 38a). It did, however, obligate the Department of the Army to assume the mortgage upon completion of the project "or upon termination of the Housing Contract for the convenience of the Department prior to completion of the project" (Pltf. Ex. No. 8, paras. 24, 29 (p. 13, *infra*)). Similar references to termination for convenience of the government were contained in the Building Loan Agreement, the Guaranty with Respect to Mortgage Payments, and the Capital Stock Escrow Agreement, all of which were collateral documents executed simultaneously with the Housing Contract.

Petitioner instituted this action in the Court of Claims to recover out-of-pocket losses and anticipated profits. The Court of Claims, in a comprehensive opinion by Judge Davis, rejected petitioner's claim for anticipated profits on the uncompleted portion of the project (Pet. App. 2a–20a). The court concluded that

[2] Plaintiff's Exhibits are contained in the original record in the Court of Claims which has been filed in this Court.

§ 8.703 of the Armed Services Procurement Regulations, 32 C.F.R. § 8.703, which directs that termination-for-convenience-of-the-government clauses "shall be inserted in all fixed-price construction contracts * * *," rendered the standard termination clause applicable to such contracts "by operation of law" (Pet. App. 18a) regardless of the contracting officer's failure to include it. The court based this conclusion on the language of the regulation and the long-standing federal policy against paying anticipated but unearned profits on defense contracts, and particularly on contracts to build military housing (Pet. App. 16a–18a). The court also observed that "termination * * * for the convenience of the Government" was referred to at least four times in the Housing Contract and collateral documents. It concluded that "[t]hese references must have had some meaning" (Pet. App. 18a), and that they must have put petitioner on notice of the government's policy regarding termination. Accordingly, it limited petitioner's recovery to the amount permitted under the clause, which did not authorize recovery for anticipated profits. Rehearing was subsequently denied in an opinion (Pet. App. 69a–87a) rejecting each of petitioner's additional contentions after full discussion.

ARGUMENT

The basic question raised by petitioner is whether § 8.703, which unconditionally requires that a termination clause be inserted in a government contract, may have the self-operative effect of binding both parties to the terms of such a clause whether or not it

is, in fact, inserted in the agreement. Having construed the particular regulation as intended to have that effect and noting the several indications in the language of the Housing Contract and accompanying documents that the parties contemplated termination for the convenience of the government, the Court of Claims correctly concluded that it was "both fitting and legally sound" to apply the standard clause to the agreement of the parties (Pet. App. 18a). Neither this conclusion nor the court's determinations relating to petitioner's subsidiary contentions require further consideration by this Court.

1. The Court of Claims correctly construed § 8.703 as mandatory. The regulation unequivocally prescribed a standard termination clause and authorized the clause's omission *only* if the contract price was under $5,000 and there was no more than a remote possibility of termination for convenience.[3] The specific exception clearly implied that in all other instances a termination-for-convenience clause was required. Moreover, as the court's survey of the history of termination provisions disclosed (Pet. App. 16a–17a), firmly-rooted reasons of policy underlie the regulation, and the draftsman could not have intended to permit *ad hoc* departures from such a consistently recognized principle of public procurement policy. Indeed, the specific procedures prescribed for "deviations" in § 1.109 of the regulations (32 C.F.R.

[3] The exception was in force at the time the present contract was entered into (Pet. App. 97a, 98a). In it's current form, the regulation applies only to contracts in excess of $10,000. 32 C.F.R. § 8.703 (rev. 1961).

§ 1.109) indicate that when such procedures are not followed the prescribed standard clauses ought to apply.

As the Court of Claims observed, "it is important * * * that procurement policies set by higher authority not be avoided or evaded (deliberately or negligently) by lesser officials, or by concert of contractor and contracting officer" (Pet. 77a). Consequently, in order to effectuate the policy established by the regulation, the court incorporated the prescribed termination clause into the agreement "by operation of law." This course was consistent with applicable decisions of this Court such as *De Laval Steam Turbine Co.* v. *United States*, 284 U.S. 61, 71–74, and *College Point Boat Corp.* v. *United States*, 267 U.S. 12, in which a right of cancellation granted by statute "became, by implication, one of the terms of the contract." 267 U.S. at 15. The fact that the termination clause in the present case was prescribed by regulation rather than by statute was properly rejected as immaterial. This Court has often held that duly authorized regulations have "the force of law." *E.g.*, *Paul* v. *United States*, 371 U.S. 245, 255; *Public Utilities Comm'n of California* v. *United States*, 355 U.S. 534, 542–543.

Petitioner's contention that this incorporation of the prescribed provision into the agreement by operation of law renders unpredictable the extent of obligations under military procurement contracts (Pet. 9–14) is without merit. The regulation which the Court of Claims applied in the present case was pub-

lished in the Federal Register, 18 Fed. Reg. 6430, and in the Code of Federal Regulations, 32 C.F.R. § 8:703 (rev. 1954). It is difficult to believe that a contractor who is responsible for the performance of a 32-million-dollar contract did not have the time or means to consult the applicable regulations published in well-known reference sources. This is particularly true when, as was the case here, the basic contract and accompanying documents make several references to termination for the convenience of the government. Any government contractor is surely aware of the existence of the Armed Services Procurement Regulations and is on notice that his contract may be governed by its applicable provisions. Hence this case involved no claim of surprise, as might arise if a regulation to which contractors had no access were applied to an existing contract. And its result cannot be considered unfair in any sense; the contractor received his profit on the 2 percent of the work which he performed.[4]

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[4] Nor was the Court of Claims' decision inconsistent with *United States* v. *Speed*, 8 Wall. 77, as petitioner contends (Pet. 7–9). *Speed* concerned a regulation of the Secretary of War relating to "contracts for subsistence stores." As did the regulation in the present case, the *Speed* regulation prescribed that all such agreements "shall" provide for their termination at the convenience of the government. The particular contract on which suit was brought failed to contain any such provision. In answer to the government's contention that because of the regulation "the agreement is to be treated as though that provision were in it" (8 Wall. at 83), the Court held that the contract was not "for subsistence stores" so that the regulation was inapplicable. The Court did not question the validity of the government's proposition that an *applicable* regulation should be incorporated into the contract by operation of law.

2. Moreover, the bare question whether a clause prescribed by an applicable regulation should be incorporated into a military procurement contract by operation of law if it is otherwise omitted is not appropriately presented by this case. Since the Housing Contract and other documents referred to termination for the convenience of the government, the Court of Claims held, on rehearing, that the standard clause set out in § 8.703 had been incorporated "by reference" (Pet. App. 75a). In light of the long-standing policy regarding termination of military procurement contracts, which must have been well-known to experienced contractors such as petitioner, this was a reasonable conclusion as to the intent of the parties. And since the case concerned only the construction of § 8.703 in light of well established procurement policy, it is of minimal significance in other cases.[5]

3. Petitioner also contends that if § 8.703 is construed to govern contracts regardless of the parties' failure to include the termination-for-convenience clause set forth in the regulation, it is without statu-

[5] The regulation being, at the very least, a binding instruction to contracting officers, there is little likelihood that the situation presented here will recur. We have been able to find only a single comparable case—*J. W. Bateson Co., Inc.* v. *United States*, Ct. Cl. No. 365-60, issued on the same day as the opinion on rehearing in this case (Pet. 69a). Neither *Homer Electric Ass'n, Inc.*, ASBCA No. 7649, nor *Aero Corp.*, ASBCA No. 8178, which are relied on by petitioner (Pet. 12), concerned contracts as to which the ASPR prescribed termination or "changes" clauses. In *Aero Corp.* the Board of Contract Appeals expressly noted that no mandatory provision was involved and further distinguished the present case because it concerned a construction of § 8.703 only. See ASBCA No. 8178, page 11, note 8.

tory authority (Pet. 16–21). However, there is ample authority for § 8.703 in the broad terms of the Armed Services Procurement Act of 1947, 62 Stat. 21, as amended, 10 U.S.C. 2301 *et seq.*, as well as in the statutes giving the Defense and Service Secretaries power to adopt regulations in their fields of competence, including procurement. 10 U.S.C. 3012, 6011, 8012. See *Priebe & Sons v. United States*, 332 U.S. 407, 413. The fact that none of these statutes refer specifically to termination of contracts for the convenience of the government does not mean that authority to issue regulations with respect to such termination does not exist.

4. Petitioner further contends that Part 8 of the Armed Services Procurement Regulations does not apply to Capehart Act projects. This question is now of limited importance, since the Capehart Act expired on October 1, 1962, and has not been renewed. 76 Stat. 418, amending 12 U.S.C. 1748b(a). Moreover, the decision of the Court of Claims in this regard was clearly correct. The Armed Services Procurement Act was intended to apply generally to military construction contracts; the existence of special legislation such as the Capehart Act, which provided additional authority for a particular type of military construction contract, did not remove that type of contract from the reach of the general provisions of the Procurement Act and the regulations thereunder.[6] And there is no merit to the contention

[6] See Section 1.101 of the ASPR (32 C.F.R. § 1.101), providing that the Procurement Regulations apply generally to procurement of supplies and services under the Procurement Act "or under other statutory authority."

that Capehart Act contracts did not "obligate appropriated funds" within the meaning of the regulatory language defining the scope of the Armed Services Procurement Regulations (Pet. 22–24). The government's obligation to assume the mortgages here involved was clearly set forth in paragraph 29 of the Housing Contract. The initial use of private funds to finance the expenses of construction does not alter the fact that the Housing Contract did "obligate appropriated funds."[7]

5. Petitioner's final contention is that the Court of Claims erroneously limited the subcontractors' rights to those which could be asserted by the prime contractor (Pet. 24–25). But this limitation was imposed by the very terms of the subcontracts, which specifically provided (Pltf. Ex. Nos. 102A–102H) that they "shall be subject to and governed in accordance with the obligation, liabilities and duties imposed by [the Capehart Act] and Housing Contract."

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[7] *Continental Casualty Co.* v. *United States ex rel. Robertson Lumber Co.*, 305 F. 2d 794 (C.A. 8), certiorari denied, 371 U.S. 922, and *United States ex rel. Miles Lumber Co.* v. *Harrison and Grimshaw Const. Co.*, 305 F. 2d 363 (C.A. 10), certiorari denied, 371 U.S. 920, on which petitioner relies (Pet. 23–24), are inapposite. Both cases concern the sufficiency of notice required to support a suit against a surety on a Capehart Act bond. While it was argued in these cases that the use of private funds in Capehart Act projects should distinguish them, for bond requirements, from Miller Act cases, the opinions are addressed to the particular problem of bonds and do not bear on the question whether Capehart Act contracts obligate appropriated funds within the meaning of the Armed Services Procurement Regulations.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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NOVEMBER 1963.

APPENDIX

Extracts from plaintiff's Exhibit No. 8, pp. HC–16 to HC–17:

(24) The eligible builder [Christian, Centex-Zachry] simultaneously with the delivery of this Housing Contract shall deposit in escrow with the mortgagee resignations of the officers and directors of each mortgagor-builder, together with certificates, endorsed in blank, representing all of the capital stock of each mortgagor-builder, for delivery to the Department [Department of the Army] upon issuance of the Determination of Completion and the final endorsement of the mortgage note for mortgage insurance by the Commissioner. [Federal Housing Commissioner], *or upon termination of the Housing Contract for the convenience of the Department prior to completion of the project.* The escrow agreement shall be in a form acceptable to the Department and the Commissioner. [Emphasis added.]

* * * * *

(29) The Department shall, to the extent that advances made against each mortgage note (identified in each Building Loan Agreement above referred to) have been approved by the Commissioner, make payments in accordance with the terms of said note, provided that this obligation to make payments shall not become effective until the Commissioner shall have finally endorsed said note for mortgage insurance, *or upon termination of the Housing Contract for the convenience of the Department prior to completion of the project.* * * * [Emphasis added.]

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